A6735-1-F

1986 State of the Convenience Store Industry

National
Association of
Convenience Stores

Foreword

The National Association of Convenience Stores has been working for more than 25 years to provide the best in member training, education assistance and services. As the convenience store industry's national representative, we're proud to add this timely report to your Association's list of publications. We feel this report represents a significant contribution to our goal of improving the data base for managerial decision-making.

NACS wishes to thank Arthur Andersen & Co., a recognized authority in the field of retail food surveys, for conducting, compiling and reporting this survey; and Gerke Economics, for writing and editing the narrative copy for this report.

Glen DeWeese
Super Stop
Vice-Chairman, Executive
Committee for Education
and Training

State of the Industry 1986
Price: NACS Members — $20.00
Non-members — $30.00

National Association of
Convenience Stores
1605 King Street
Alexandria, Virginia 22314-2792
(703) 684-3600

Copyright © 1986 National
Association of Convenience Stores, Inc.

Printed in U.S.A.

Highlights

Industry Totals

Stores	61.0 Thousand
Total Sales	$54.2 Billion
Gas Sales	$18.2 Billion
Non-Gas Sales	$36.0 Billion
Profits	$1,463 Million
Number of Employees	397 Thousand

Industry Trends
(Change from 1984)

Stores	+ 6.5%
Sales	+ 14.1%
Profits	+ 4.5%

Industry Averages

Sales Per Store Non-Gas	$590,000
Sales Per Store Gas	$542,000
Investment Required for New Urban Store	$597,700
Sales Per Customer	$2.07
Gross Profit Margin Non-Gas	32.2%
Gross Profit Margin Gas	7.3%
Gross Profit Margin Combined	22.8%
Profit Before Taxes	2.7%
Convenience Store Inflation Rate	3.1%
1985 LIFO Savings Per Store	$900

About This Study

The NACS "State of the Convenience Store Industry Report" has become a recognized publication that presents reliable and up-to-date industry data. NACS is once again distributing this annual State-of-the-Industry report in the belief that this data base will help increase the quality and improve the accuracy of business decisions throughout the convenience store industry.

A total of 140 companies that operate 21,870 store units (approximately 48% of the stores on the NACS membership roster) responded to our request for various types of statistical information. This compares to a sample size of 131 companies and 20,535 stores last year.

We believe that the data we have amassed in compiling this report paints a highly realistic portrait of our industry and serves as a valid indicator of how it has coped with the climate in which it operated throughout 1985.

Following the procedure instituted in developing data for prior reports, we again mailed a condensed questionnaire to "A" size companies (1-10 stores). An independent profile is presented in a separate section of this report. The survey of companies of larger size was based on the more extensive questionnaire which was revised to facilitate completion.

A word about the statistical validity of our findings. In surveys of this type, responding companies differ from year to year and so direct comparability is never entirely possible. We believe, however, that the conclusions drawn from this survey provide an accurate picture of the State of the Convenience Store Industry.

In addition, all the figures in this report are averages based on the number and size of the companies participating in the survey. In calculating averages, each company's response and specific survey question has been weighted according to the relationship of its size to the aggregate size of all reporting companies. As a result, the sample size of each response presented herein will vary. Past year's data have been presented to the extent that such information was presented last year or information relating to new questions was available.

Arthur Andersen & Co., long recognized for its expertise in retail food surveys, has assembled all the data in this report. Arthur Andersen & Co. and NACS feel that the sheer number of responses is highly representative of the state of the industry in 1985 and provides the research reliability desired by NACS Members.

Additionally, all company responses have been kept strictly confidential by Arthur Andersen & Co.

Table of Participation

NACS Directory

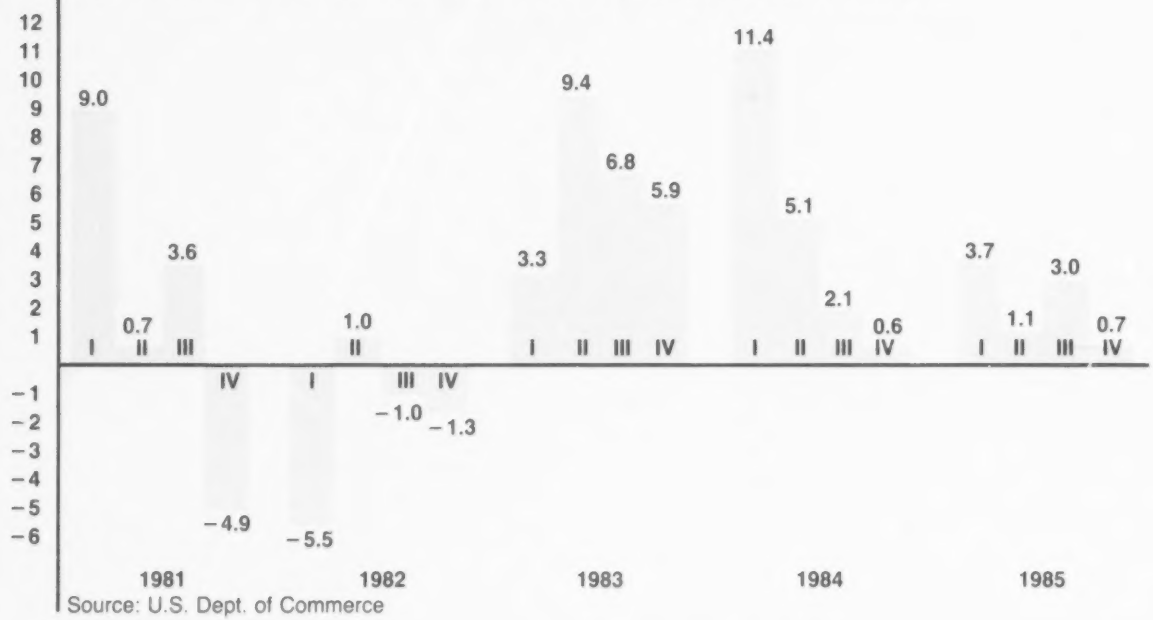
Classification	Number of Stores	As of 12/31/85 Number of Members	As of 12/31/85 Number of Stores	Number of Useable Responses	Number of Stores
A	1-10	665	3,058	76	466
B	11-50	342	7,257	21	414
C	51-200	105	10,668	23	2,220
D	201-500	18	5,943	13	4,285
E	Over 500	11	18,902	7	14,485
		1,141	45,828	140	21,870

Nineteen Hundred Eighty-Five

The economy enjoyed a third consecutive year of growth in all four quarters. The rate of growth did slow from the previous two years. Even with the lower rate of economic growth, the future prospects for business are encouraging.

Employment has stabilized at a level many feel is nearing full employment. Inflation forces are under control. Interest rates have returned to levels that permit business activity to prosper. Real disposable income is continuing to rise.

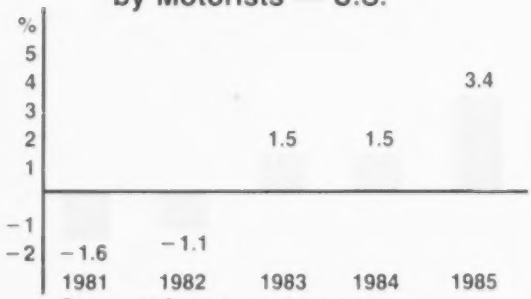
Fig. 1—Real Gross National Product Quarterly Percent Change



Source: U.S. Dept. of Commerce

The petroleum production industry continues to suffer under the weight of heavy world crude supplies. While domestic gasoline production has declined, the increasing demand for gasoline has been met. The market trend of increased motorist consumption established in 1983 continues at an accelerating rate. The market has not recovered to the volume levels of the late 1970's and early 1980's. However, when the increased fuel efficiency of new automobiles is taken into consideration, the volume which has been regained is substantial.

Fig. 2—Annual Percent Change in Gallons of Gasoline Used by Motorists — U.S.



Source: U.S. Highway Administration
(Preliminary Estimate for 1985)

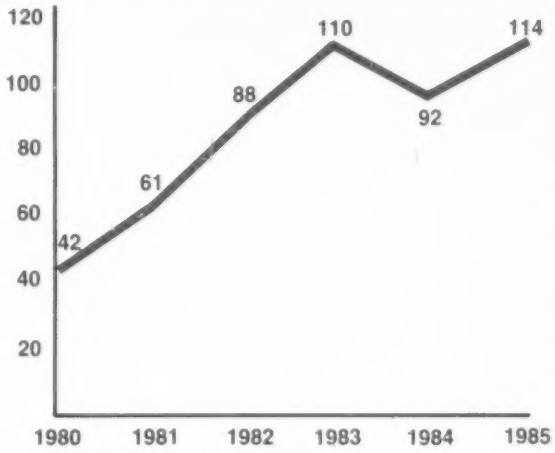
Business

The slowing of economic growth and disinflation have directly affected many businesses. The most recent figures compiled by Dun and Bradstreet show that 114 businesses out of every 10,000 failed in 1985. This was an 18.8% increase in the rate of failure over 1984 and set a new historical high. Retail trade and wholesale trade businesses were bright spots as the total number of failures in 1985 actually decreased by 2.3% from 1984. More than offsetting failures were new business incorporations which increased 5.4% in 1985. The U.S. business economy continues its transition.

Workers

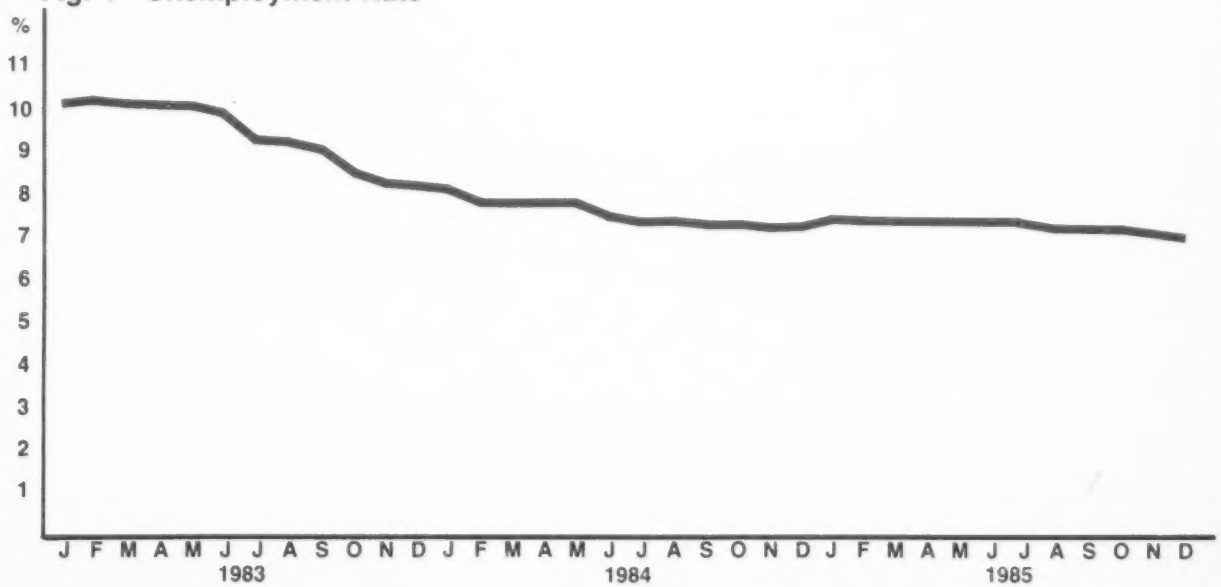
The stable unemployment rate established in the last half of 1984 carried through into 1985 maintaining a 7.3% level through the summer and taking a traditional season dip to 6.9% during the fall. Contributing to the stable employment level was a 5.8% increase in personal income which outpaced the consumer price increase of 3.6% during 1985.

Fig. 3—U.S. Business Failures Per 10,000 Businesses



Source: Dun and Bradstreet

Fig. 4—Unemployment Rate



Source: Bureau of Labor Statistics

Prices

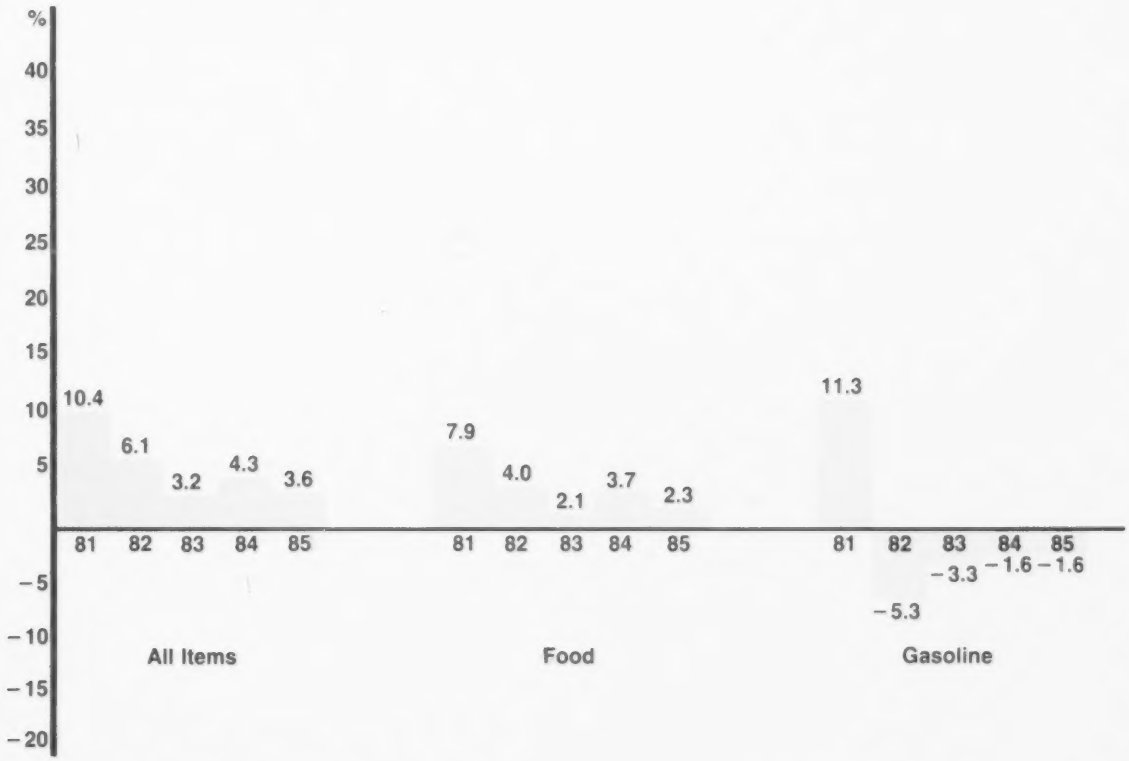
Inflation remained under control in 1985. Consumer prices increased by only 3.6%, the second smallest increase in the last ten years and well below the double digit inflation rates of the late 70's and early 80's.

Food became more of a bargain for the consumer as the annual price increase of 2.3% fell well below the increase in personal income, 5.8%, and the general increase in total prices.

The oversupply of world crude has contributed to a fourth consecutive year of lower gasoline prices at the pumps. 1985 matched the 1.6% price reduction of 1984. As previously noted, this price reduction has directly contributed to an even larger volume demand for gasoline and total gasoline sales. In addition to benefitting the motorist, reduced transportation and production costs have further supported business activity.

From the perspective of the food and gasoline retailer, greater pressure was placed on business as operating costs continued to rise faster than selling prices.

Fig. 5—Inflation (Deflation) Rate
Annual Percent Change

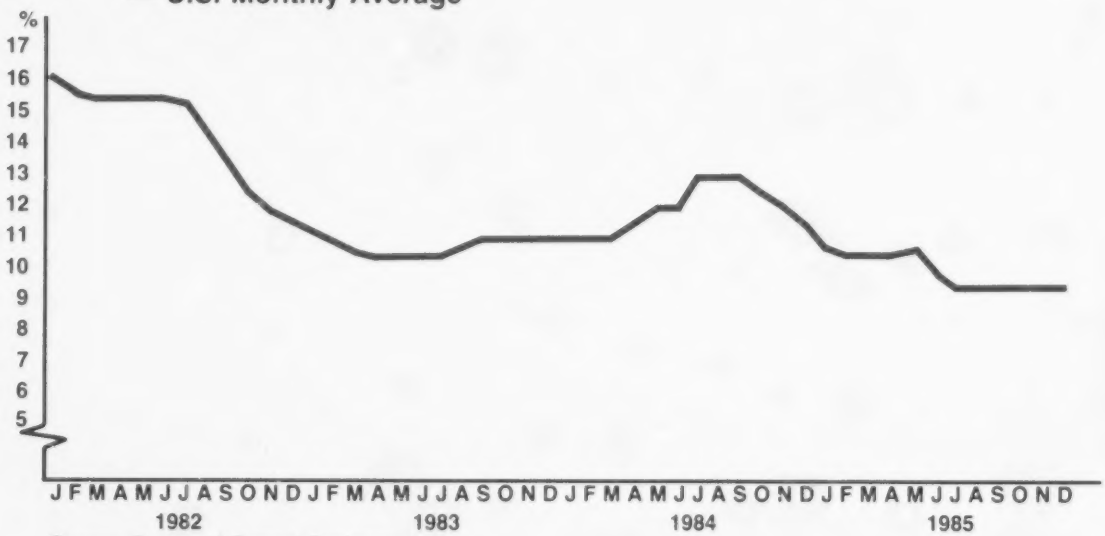


Source: Consumer Price Index

Finance

Interest rates eased further as inflation remained under firm control and economic confidence grew stronger. The annualized prime rate for 1985 of 9.9% was more than 2 percentage points below the annualized prime rate of 1984. With the prime rate falling below double digits for the first time in the 1980's, unemployment stabilized, consumer and business borrowings and investment increased, and general demand for goods and services continued to pick up.

Fig. 6—Prime Rate Charged by Banks — U.S. Monthly Average

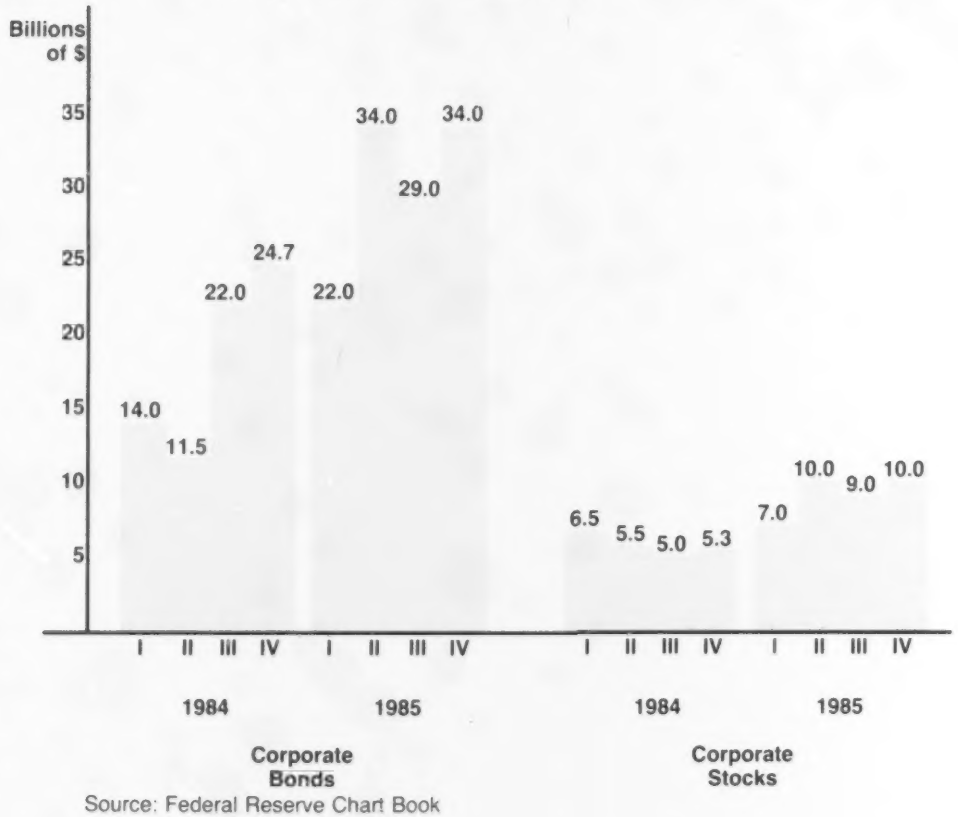


Source: Survey of Current Business

Corporate bond yields, Aaa rating, declined an additional 3% during 1985. Business responded to lower short-term and long-term rates by increasing bond offerings by more than 50% over 1984's level and stock offerings by more than 30%. Corporate acquisitions and mergers reached the highest level of activity in over 50 years.

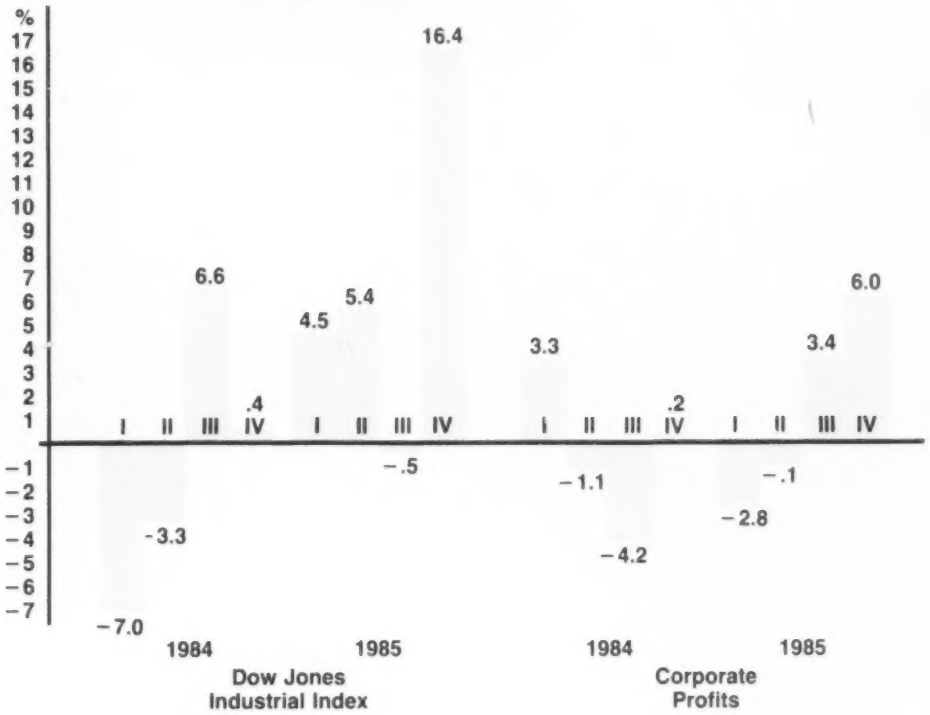
Consumers responded in similar manner to the prospect of continued prosperity. Consumer installment credit outstanding increased from $460.5 billion at the end of 1984 to an ending 1985 level of $550.4 billion, a 19.5% increase. The consumer provided both the capital needed for business and helped fuel the demand for business output. Total personal consumption rose by 6.6%, nearly one percentage point higher than the rise in personal income and three percentage points higher than consumer price increases.

Fig. 7—Corporate Security Issues Gross Proceeds — Quarterly



Source: Federal Reserve Chart Book

Fig. 8—Quarterly Percent Change
—Dow Jones Industrial Index
—Corporate Profits

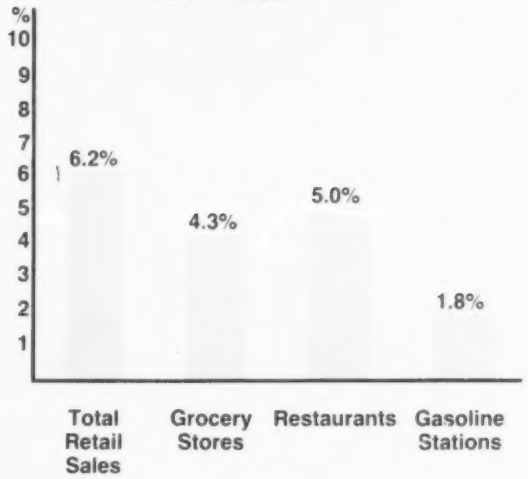


Sources: Dow Jones, Federal Reserve

Sales

Consumer confidence and increased consumption were directly reflected in total retail sales which were 6.3% higher than 1984. Durable goods, up 10.0%, was the strongest factor. However, non-durable goods also benefited from increased consumption. Both grocery sales, up 4.3%, and restaurant sales, up 5.0%, outpaced the 3.4% growth in the gross national product. A 1.8% increase in gasoline service station sales was respectable after a 2.1% decline in 1984 and a 1.6% additional reduction in gasoline selling prices.

Fig. 9—Percent Change in Retail Sales 1984 - 1985



Source: U.S. Census Bureau

Change

1985 was a year of economic stabilization. The growth rates of the previous two years slowed to more historically normal rates as inflation remained under control, interest rates returned to single digits on short term loans, and fuel costs declined further. Consumer confidence continued to build with increased levels of spending and consumption. The market for investments began to pick up sharply as business activity and profits made substantial headway. But these are challenging times for management.

Convenience store industry executives have learned to prosper during disinflation and even deflation. They are coping with sky-high insurance costs, underground storage tank liabilities and consumer group pressures regarding alcoholic beverages and adult magazines. They are facing increased and changing competition, a changing labor force, and the uncertain opportunities of new technology.

Executives throughout the industry are searching for better information to more efficiently manage their businesses. One source of valuable information is this report on the State of the Convenience Store Industry.

Industry Sales and Profits

Total sales for the nation's 61,000 convenience stores was $54.2 billion in 1985 — a healthy 14.1% over 1984. This compares favorably to the 6.2% increase on all retail sales for 1985.

Slightly less than one-half of the increase in industry sales came from adding new stores. The industry had a net increase in stores of 6.5%.

Industry gasoline sales increased 11.7% to $18.2 billion. Total gasoline station sales in the U.S. increased only 1.8% in 1985.

In-store sales for the convenience store industry were $36.0 billion in 1985. This was 15.4% above 1984. The 1985 sales increases for all grocery stores and restaurants were 4.3% and 5.0%, respectively.

The sales increases more than offset a slight decline in the net profit percent. Before-tax profits for the convenience store industry increased 4.5% to $1,463 million, but average store profits dropped slightly to $24.0 thousand in 1985 compared to $24.8 thousand in 1984. The 1985 per store profit is still considerably higher than the profit performance of the early 1980's.

Total industry employment showed an increase of 8.0% to 397,000 people. This number includes full-time and part-time store employees, supervisory personnel and corporate staff.

Fig. 10—Total Convenience Store Industry Sales

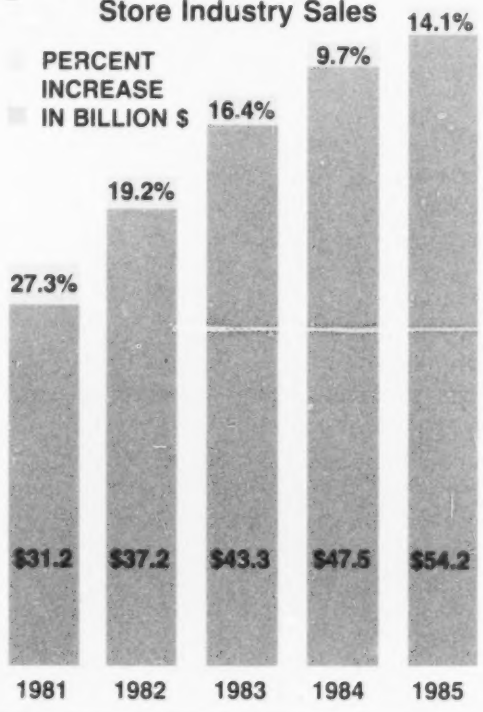


Fig. 11—Total Non-Gas vs. Gas Sales

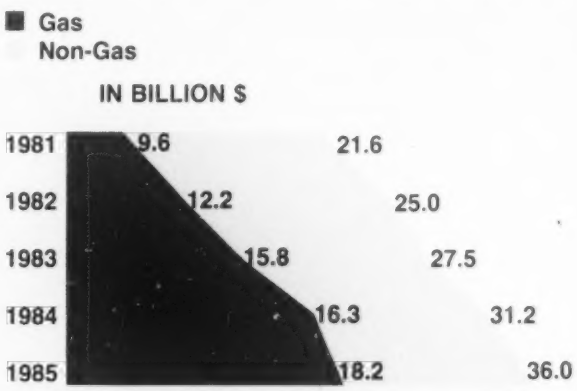


Fig. 12—Total Convenience Store Industry Profit Before Taxes

(in millions)

Sales and Profits Per Store

We are pleased to present for the first time in 1986 summarized Profit and Loss Information. Comparative profit and loss information will be included in subsequent reports. As shown in Figure 14, gross margin increased as size increased. Store operating expenses, however, also increased with size, thereby narrowing the gap in store operating profit among the Group "B", "C", "D", and "E" companies. With the exception of Group "D" companies, corporate general and administrative expenses followed the same trend.

The reason Group "B" companies' margins and expenses were lower was that a larger percentage of company revenues came from gasoline. The Group "E" companies' higher margin may be due to the fact that most companies in this size group have warehouses for distributing products. Less than half of the "B", "C", and "D" companies warehouse any products.

1985 continued to show a healthy growth in average yearly store sales (excluding gas), coupled with continued improvement in gross margins for both gas and non-gas sales.

The 1985 $590,000 average yearly stores sales (excluding gas) is another historic high for the industry. For stores selling gasoline, average gasoline sales were $542,000 in 1985. The average gross margin of 22.8% is the highest since 1981's margin of 22.9%.

Unfortunately, however, the industry was unable to flow the increased margins to the bottom line, as pretax profit as a percent of sales (including gas) fell to 2.7% in 1985 from 3.1% in 1984. With the exception of the Group "D" companies, all groups showed a decrease. The reduction in the percentage of pretax margin is primarily attributable to increased insurance expenses and depreciation. In the Business Costs section of this report, we address the effect of the "insurance crisis" on the cost of insurance and the effect of the substantial investment required for new stores on depreciation. To a lesser extent, increased labor and store operating costs also adversely affected the pretax margin.

Merchandising is a key ingredient for the successful operations of convenience stores. Merchandising programs nave the two-fold objective of increasing store traffic and increasing the average sale per customer.

1985 shows an increase in total store traffic and in the average sale per customer, a continuation of the trend from 1982.

The average sale of $2.07 per customer in 1985 has exceeded the 1981 level of $2.05, with all groups showing an increase over 1984. Due to the limited response of Group "E" companies in 1984, we were unable to provide an average for the Group "E" companies.

Fig. 13—Profit Before Taxes Per Store

Fig. 14—1985 Profit and Loss Information

	B	C	D	E	AVG.
Non-Gas Sales	36%	47%	51%	50%	46%
Gas Sales	64	53	49	50	54
Total Sales	100%	100%	100%	100%	100%
Cost of Goods Sold	83.5	80.4	79.9	74.3	77.2
Gross Profit	16.5	19.6	20.1	25.7	22.8
Direct Store Operating Expense	12.9	14.7	15.1	18.7	16.9
Store Operating Profit	3.6	4.9	5.0	7.0	5.9
Corporate G&A	(2.5)	(3.4)	(2.7)	(4.1)	(3.5)
Other Income	.6	1.0	.8	1.5	1.2
Other Expense	(.3)	(.8)	(.6)	(1.2)	(.9)
Pretax Profit	1.4%	1.7%	2.5%	3.2%	2.7%

Fig. 15—Average Yearly Store Sales (excluding gas) and Percentage Increase Over Previous Year

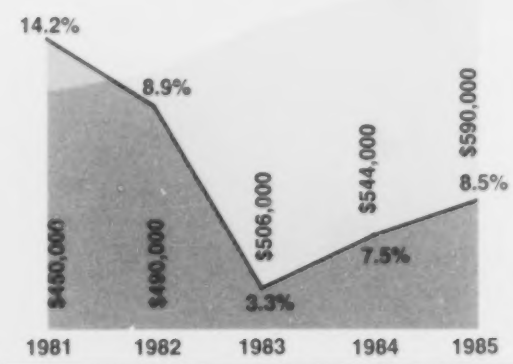


Fig. 16—Gross Margin as a Percent of Sales

1981	Average 22.9	Gas	4.2
		Non-Gas	31.8
1982	Average 20.8	Gas	4.5
		Non-Gas	30.1
1983	Average 20.7	Gas	5.0
		Non-Gas	31.5
1984	Average 21.6	Gas	6.0
		Non-Gas	32.0
1985	Average 22.8	Gas	7.3
		Non-Gas	32.2

Fig. 17—Pretax Profit as a Percent of Sales (includes gas) by Classification Group

Group	1981	1982	1983	1984	1985
B	3.8%	3.4%	1.5%	1.7%	1.4%
C	2.1	2.4	2.1	1.8	1.7
D	3.0	1.8	1.7	2.3	2.5
E	3.0	1.5	2.6	3.3	3.2
Average	2.8	2.0	2.2	3.1	2.7

Fig. 18—Average Yearly Store Sales (excluding gas) by Classification Group

Group	1981	1982	1983	1984	1985	1985% Increase
B	$319,000	$365,000	$370,000	$408,000	$397,000	(2.7)%
C	377,000	429,000	440,000	431,000	439,000	1.9
D	354,000	380,000	378,000	436,000	470,000	7.8
E	495,000	539,000	558,000	588,000	649,000	10.4
Average	450,000	490,000	506,000	544,000	590,000	8.5

Fig. 19—Average Sale Per Customer (excluding gas) by Classification Group

Group	1981	1982	1983	1984	1985
B	$1.92	$2.55	$2.18	$2.69	$2.40
C	1.77	1.81	1.89	2.04	2.22
D	1.90	1.97	1.99	1.98	2.14
E	2.15	2.03	2.09	N/A	1.91
Average	2.05	1.99	2.00	2.04	2.07

Store Development

Store growth showed a net increase of 6.5% for 1985. This reverses a four-year trend of declining growth in the convenience store industry. The total number of stores in the industry rose to 61,000.

The increase in the investment required for new stores continues unabated. The critical evaluation of existing and potential profitability is a necessity. With the investment required for new stores as shown in Figure 21, the analysis of individual store profitability becomes increasingly important. Annual sales for new stores will need to exceed the averages for existing stores by a sizeable amount to insure the recovery of this investment.

The percentage increase in the cost of both urban and rural stores in 1985 over 1984 exceeded the percentage increase of 1984 over 1983. For urban stores, 1985 showed a 20% increase over 1984; this compares to 10% for 1984 over 1983. For rural stores, the 1985 increase was 15% compared to 4% for 1984.

For urban stores, cost increases were substantial in all categories. The cost of land, however, is astonishing, increasing 60% since 1982 for the urban store and 94% for the rural store. The rural store received a respite, at least for 1985, with land cost approximating that of 1984.

It is not surprising to see the increase in the level of inventories for new urban stores, which are required to support the higher annual sales that must be generated to insure an adequate return on investment. The increase in the cost of the rural stores continues to reflect the emphasis being placed on this market. The saturation of the urban market is evident in the costs required for new urban locations.

The rural stores showed a substantial increase in the 1985 cost of gas equipment over 1984 and exceeding the comparable cost required for urban stores. This may be the result of larger rural land parcels over that of the urban stores with a corresponding increase in the size of rural gasoline operations.

Fig. 20—Store Growth Analysis

	1981	1982	1983	1984	1985
New Stores Opened	11.2%	10.2%	7.6%	7.3%	8.0%
Acquired Stores	1.7%	0.8%	2.7%	2.9%	3.6%
	12.9%	11.0%	10.3%	10.2%	11.6%
Stores Sold or Closed	(4.3%)	(4.1%)	(4.1%)	(4.8%)	(5.1%)
Net Increase in Stores	8.6%	6.9%	6.2%	5.4%	6.5%
Actual Number of Stores (000's)	47.9	51.2	54.4	57.3	61.0

Fig. 21—Investment per New Store

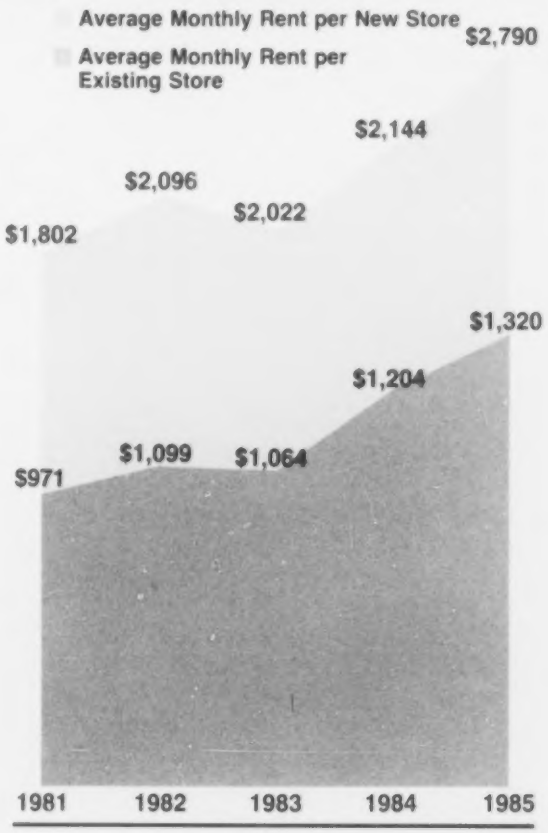
		1982		1983		1984		1985	
		Urban	Rural	Urban	Rural	Urban	Rural	Urban	Rural
	Land	$133,400	$ 57,100	$147,900	$ 89,800	$170,200	$108,700	$212,800	$110,800
	Building	101,400	91,600	125,300	101,700	149,800	106,900	180,000	118,900
Equipment	Fast Food	17,900	11,000	14,200	7,700	14,100	9,100	19,000	16,200
	Gas	46,300	34,600	59,900	50,000	55,100	49,400	65,700	73,700
	Non-Gas	70,700	38,800	53,600	48,000	61,000	39,300	63,300	48,100
	Total	134,900	84,400	127,700	105,700	130,200	97,800	148,000	138,000
	Inventory	47,500	39,100	50,000	45,000	46,000	42,800	56,900	43,100
	Total Investment	$417,200	$272,200	$450,900	$342,200	$496,200	$356,200	$597,700	$410,800

There was little change in the average square footage of the urban store — 2,558 compared to 2,530 in the prior year. There was also little change in the average square footage of the rural store — 2,491 compared to 2,516 in the prior year. The average square footage of new stores was reported to be 2,427 compared to 2,469 in the prior year. The average lot size of new stores was 23,360 square feet compared to 23,717 square feet for existing stores.

The average monthly rent increased for both the new store and for the existing store. Based upon the reported increase in the investment required for a new store, it is not surprising to see a comparable increase in average monthly rents for new stores. Compared to 1984, the increase in the average monthly rents for existing stores appears surprising. However, 1983 reported a decrease from 1982. The increase in the average monthly rents for existing stores is probably affected by the cost of new stores, with investors setting rent levels based on the current cost of land acquisition and store construction.

Approximately 23% of existing stores are owned and 77% are leased, about the same as 1984. For new stores, however, approximately 37% are owned compared to 49% reported in 1984.

Fig. 22—Average Monthly Rent



Business Costs

Although sales and margins increased, pretax profit (including gas) decreased to 2.7% of sales in 1985. Increases in sales and gross margins will not flow to pretax profit unless expenses are controlled and maintained proportionately to sales. An analysis of selected expenses as a percent of non-gas sales and total sales in Figure 24 shows an increase in all categories except general and administrative. These increases more than offset the improvement in gross margins resulting in a decrease in the percentage of pretax profit.

Labor was the largest expense component of the selected expense profile and represented a large factor in the reduction in the percentage of pretax profit. As discussed later in this section, insurance and depreciation showed the largest percentage increase over 1984.

Although the average monthly utility cost per store rose to $1,107, an increase of 10% over 1984, it represented only a .1% increase as a percentage of sales. The recent volatility of energy costs makes it difficult to evaluate the results of the energy efficient programs introduced just several years ago.

General and administrative expenses registered a decrease from 6.6% to 6.1% of non-gas sales and from 3.9% to 3.6% of total sales from 1984 to 1985. As a percentage of sales, these expenses have been brought back to 1982 levels. With the exception of Group "C" companies, all groups shared in the reduction of such expenses.

As discussed in the introduction to this report, the average prime rate for 1985 was more than 2% lower than in 1984. Business responded to the single digit interest rates with increased borrowings. Our industry statistics appear to confirm this assessment as interest expense as a percentage of both non-gas and total sales increased to 1.2% and .8%, respectively.

Fig. 23—Average Monthly Utility Cost per Store

Fig. 24—Selected Expense Profile as a Percent of Non-Gas and Total Sales

			1983		1984		1985	
	1981	1982	Non-Gas	Total	Non-Gas	Total	Non-Gas	Total
Labor	12.9%	12.9%	12.7%	7.5%	12.2%	7.0%	12.6%	8.0%
General & Administrative	5.9	6.2	6.6	3.6	6.6	3.9	6.1	3.6
Utility	2.5	3.1	3.2	2.0	3.0	1.8	3.1	1.9
Advertising	.4	.6	.4	.2	.4	.3	.6	.4
Interest Expense	.5	.6	1.1	.5	1.0	.7	1.2	.8

Fig. 25—General and Administrative Expenses by Classification Group

Group	As a % of Non-Gas Sales					As a % of Total Sales				
	1981	1982	1983	1984	1985	1981	1982	1983	1984	1985
B	6.2%	5.9%	8.2%	6.6%	5.7%	3.0%	3.4%	3.2%	3.0%	2.5%
C	7.9	5.5	6.0	5.9	7.3	4.4	3.3	3.3	3.0	3.4
D	5.9	7.8	7.2	6.9	5.4	3.4	3.6	3.2	3.0	2.7
E	4.7	5.0	6.2	6.8	6.1	3.9	3.6	4.1	5.0	4.1
Average	5.9	6.2	6.6	6.6	6.1	3.9	3.6	3.6	3.9	3.6

As labor represents the largest single expenditure, the ability to maintain the average number of employees is crucial to cost control. Information relating to the average number of employees per store and the average number of non-store employees, therefore, continues to be of interest. The 6.5 average number of total employees (store and non-store employees) per store (6.4 in 1984) is the result of an increase in the average number of store employees per store to 6.0 in 1985 from 5.9 in 1984. The average number of non-store employees remained constant at .5. Figure 26 presents a breakdown of the average number of employees among all group companies. The slight increase in the average number of employees per store is consistent with the increase in the average annual sales per store.

Reported non-gas inventory shrinkage for the industry was 1.0% of non-gas sales in 1985 compared to .8% in 1984. Group "B" companies reported inventory shrinkage of .9% (no change from 1984); Group "C" companies 1.3% (.8% in 1984); Group "D" companies .7% (.6% in 1984); Group "E" companies 1.1% (.9% in 1984).

Industry averages for insurance and taxes increased 16% over the reported amounts for 1984 with increases being reported by all group companies. We are all aware of the "insurance" crisis and the 16% increase does not seem out of line with the overall increases being passed on to all industries by insurance companies.

Depreciation jumped a sharp 29% for the total industry over 1984. As with insurance and taxes, such increases were experienced by all group companies. It is not surprising to see a sizeable increase in depreciation expense due to the significant increase in the cost of new buildings and equipment over the past several years, as is reported in Figure 21, "Investment Per New Store."

Fig. 26—Employees

Group	Average Number of Store Employees Per Store		Average Number of Non-Store Employees		Average Number of Employees Per Store	
	1984	1985	1984	1985	1984	1985
B	6.7	7.1	.5	.7	7.2	7.8
C	6.9	6.4	.8	.7	7.7	7.1
D	6.5	8.3	.7	.6	7.2	8.9
E	5.7	5.2	.4	.4	6.1	5.6
Average	5.9	6.0	.5	.5	6.4	6.5

Fig. 27—Fixed Store Expenses by Classification Group

Group	Insurance and Taxes					Equipment Depreciation				
	1981	1982	1983	1984	1985	1981	1982	1983	1984	1985
B	$3,500	$2,100	$3,300	$4,100	$5,100	$5,700	$7,200	$8,000	$8,500	$ 9,800
C	3,200	3,200	3,300	3,900	4,400	6,500	7,000	7,900	9,100	11,000
D	2,900	3,800	3,900	3,800	4,600	4,300	6,900	8,700	7,500	9,000
E	3,800	2,600	3,900	4,600	5,200	3,400	3,900	8,000	8,800	12,400
Average	3,300	3,200	3,800	4,200	4,900	4,500	5,900	8,000	8,600	11,100

Inflation and LIFO

Consumer Price Index

Inflation continues to remain under control . . . for now. The 3.6% inflation rate in 1985 is down from 4.3% in 1984 and raises no undue concern. The 1985 inflation rate reflects the stability of energy, interest and food costs. Figure 28 compares the overall rate by quarters as measured by the Consumer Price Index (CPI). The Index assumes a typical "market basket" of goods and services purchased by consumers.

Fig. 28—Consumer Price Index "Cost of Living" Increases

	1981	1982	1983	1984	1985
1st Quarter	10.6%	3.3%	0.0%	4.4%	4.3%
2nd Quarter	9.3	6.0	5.1	4.3	4.4
3rd Quarter	11.4	7.8	4.9	4.4	2.7
4th Quarter	5.8	.4	3.5	2.9	3.6
Average per Year	10.4	6.1	3.2	4.3	3.6

The CPI inflation rate is heavily influenced by energy prices, home mortgage rates and other factors that are not part of the convenience store inflation rate which is based on changes in inventory prices.

During 1985, the inflation rate for convenience store products was approximately 3.1% compared to 3.9% in 1984. The CPI inflation rate for food products was 2.3% in 1985 compared to 3.7% in 1984.

LIFO

LIFO is an inventory costing technique which charges the most recent cost of goods to cost of sales and thereby reduces the reported profits in an inflationary period.

Approximately 52% of the convenience store companies reporting (representing 78% of all stores) now use LIFO to value their inventories. Some 24% of Group "B" companies, 65% of Group "C" companies, 69% of Group "D" companies, and 60% of Group "E" companies currently are on LIFO.

The inventory inflation rate reported by operators using the LIFO method of inventory was 1.8% based on a mixture of fiscal year-ends and different product mixes. Based on the 1.8% reported LIFO inflation rate and assuming a non-gas inventory investment of $50,000, a company using the LIFO method would report approximately $900 less pre-tax profit per store. Assuming a composite Federal and state income tax rate of 50%, companies on LIFO would have increased 1985 cash flow by about $450 per store on their non-gas inventory alone.

Fig. 29—Percentage of Total Companies Using LIFO for Non-Gas Inventory in 1985

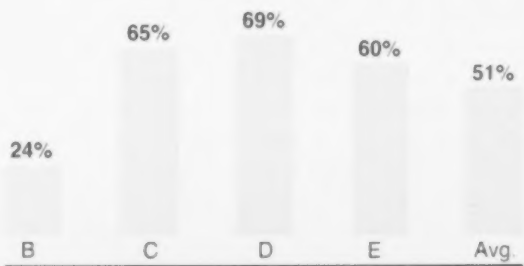


Fig. 30—Percentage of Companies Using LIFO for Gas Inventory in 1985

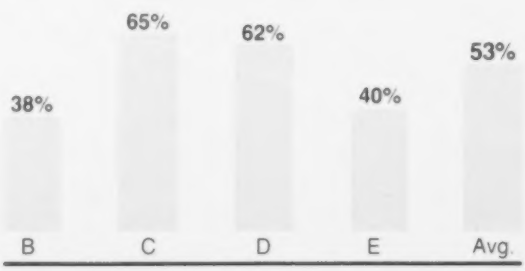


Fig. 31—Percentage of Stores Selling Gas

The average margin per gallon of gasoline continues to be unpredictable. The average gross margin on a gallon of company-owned gasoline increased to 8.0 cents in 1985 from 7.4 cents in 1984. Although not as good as company-owned gasoline, the gross margin on commission pump gasoline increased in 1985 to 4.6 cents per gallon from 3.6 cents per gallon a year earlier. Overall, the average gross margin on gasoline increased in 1985 to 7.6 cents per gallon from the 6.9 cents per gallon reported in 1984.

The percentage of stores selling gas increased to 55%. This increase may be attributable to the increase in the average margin per gallon. The average percentage of new stores with gas also showed an increase to 69%, although slightly below the 74% level of 1982. All classification groups reported a sharp increase in their percentage of new stores with gas.

Fig. 32—Average Margin per Gallon (in cents)

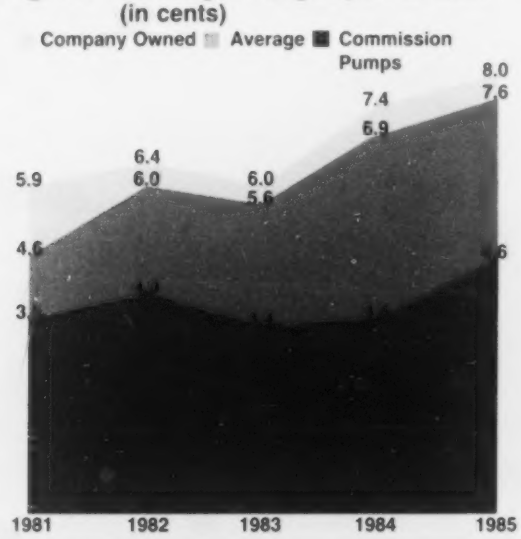


Fig. 33—Percentage of New Stores with Gas by Classification Group

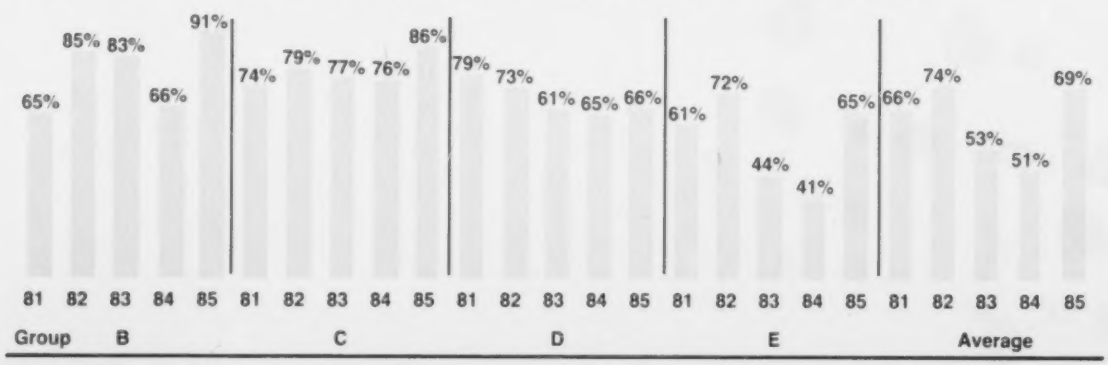


Fig. 34—Average Monthly Gallons Sold Per Store

Fig. 35—Average Monthly Gallons Sold Per Store by Classification Group

Group	1981	1982	1983	1984	1985
B	43,000	36,000	37,000	46,000	52,000
C	61,000	43,000	37,000	44,000	49,000
D	25,000	37,000	49,000	52,000	45,000
E	33,000	37,000	41,000	40,000	37,000
Average	36,500	38,000	43,000	42,000	41,000

Average monthly gallons sold per store is shown by classification group in Figure 35. Fuel pumped by the average store decreased slightly to 41,000 gallons in 1985 from 42,000 gallons in 1984. This decrease is attributable, in part, to the fact that some companies with "super pumper" operations did not provide gasoline data for 1985. Also, recent mergers in the industry may have distorted the averages for Group "D" and "E" categories.

The average sale per customer rose to $9.31 in 1985 from $8.00 in 1984. The average selling price per gallon remained at the 1984 level of $1.10. This reported increase, therefore, was due to a change in the sample of companies responding to this question in the State of the Industry Survey in 1985 versus 1984.

Of the total number of stores selling gas, 89% are company-owned and 11% are operated on a commission basis. As reported in prior years, the percentage of company-owned stores selling gas continues to increase. The average number of hoses per store was 6 compared to 5 in 1984. 54% of all stores had canopies in 1985, up from 48% in 1984.

Sales of branded gasoline continued to rise, representing 54% of total sales compared to 49% in 1984, with the unbranded gasoline comprising 46% compared to 51% in 1984. Approximately 31% of all sales were prepay, down from 38% in 1984.

The percent of gasoline installations with automated dispensing and island card readers was a new survey question in 1984. Less than 1% of those reporting in both 1984 and 1985 had such equipment. Thus, there has been no reported increase in the use of such equipment and actual use to date has been minimal.

Fig. 36—Percent of Surveyed Convenience Stores Offering the Following by Classification Group:

	B			C			D			E			TOTAL		
	1983	1984	1985	1983	1984	1985	1983	1984	1985	1983	1984	1985	1983	1984	1985
Microwave Equip.	80%	85%	92%	80%	82%	94%	83%	89%	74%	95%	99%	99%	88%	95%	93%
Money Order	40	35	25	49	48	54	79	83	55	84	81	94	74	76	80
Check Cashing	63	42	61	49	51	59	87	72	64	63	94	72	66	84	69
Fountain Drinks	64	74	82	64	63	85	95	96	89	76	98	99	78	92	95
Open 24 Hours	40	36	46	51	42	43	53	71	63	62	83	91	57	75	79
Prepared Foods	48	61	55	29	43	35	60	64	42	78	38	85	63	42	70
Service Deli	38	43	23	38	28	22	25	33	31	39	18	21	35	22	23
Film Processing	19	9	18	8	6	9	2	4	4	1	0	0	3	1	2
On Premise Bakery	5	6	4	4	7	8	2	1	9	3	1	1	3	1	3
Fried Chicken	20	8	8	2	5	8	5	4	3	2	2	0	3	3	2
Video Games	60	35	27	58	47	45	70	70	43	63	85	84	64	76	73
Automated Tellers	0	1	1	2	2	2	3	21	12	4	11	14	3	11	12
Vending Machines	18	6	4	14	6	4	2	8	5	15	1	1	12	3	3

Marketing and In-Store Merchandising

The top selling products in convenience stores were tobacco, beer and soft drinks. The 1985 results showed some changes in sales mix. Most notable was a drop in grocery sales as a percent of total sales. Conversely, all fast food product categories showed increases in distribution. (Note: Part of the year-to-year change in sales mix is probably due to a change in the sample of companies reporting.)

This year, for the first time, a sufficient sample of companies reported gross margin percentages. Figure 38 shows the average industry margins for 29 different product categories.

Compared to 1984, more stores in 1985 sold money orders, stayed open 24 hours, offered film processing and had automated teller machines. More stores also reported food service offerings of fountain drinks, prepared foods, service delis and bakeries. Although not included in Figure 36, several companies reported their stores had video movie rentals.

Fewer stores in 1985 reported having microwave equipment, check-cashing, fried chicken and video games.

More than one-third of the companies (36.5%) reported distributing some products through their own warehouse. The type of products warehoused varied by the company.

Fig. 37—Percent of Non-Gas Purchases by Product Group—Industry Average

	1983	1984	1985
Cooler			
Beer (Hot & Cold)	14.6%	13.7%	13.9%
Soft Drinks (Hot & Cold)	11.8	11.3	10.2
Juices	0.9	0.8	1.0
Milk & Milk Products	6.9	6.9	6.6
Packaged Deli	1.1	1.3	1.2
Produce	0.3	0.4	0.4
Eggs	0.3	0.4	0.4
Frozen			
Frozen Food	0.6	0.7	0.7
Ice Cream	1.5	1.6	1.6
Ice	1.0	0.9	0.9
Room Temp.			
Bread & Cakes	4.2	4.0	3.5
Cookies	0.8	0.8	0.8
Salty Snacks (Chips, Nuts, etc.)	3.5	3.8	3.7
Candy & Gum	4.9	4.9	4.9
Groceries	9.2	9.0	5.9
Health & Beauty Aids	3.4	3.3	3.4
Tobacco	17.6	18.1	17.8
Publications	4.0	4.0	5.4
Wine/Liquor	1.1	1.3	1.3
Automotive/Motor Oil	1.0	0.8	0.7
General Merchandise	2.4	2.3	2.6
Fast Food			
Sandwiches — Fresh	1.4	1.7	1.7
Sandwiches — Frozen	0.9	1.2	1.4
Deli Services (excluding sandwiches)	2.0	1.3	3.0
Food Cooked On-site	0.3	0.2	0.3
Fountain Drinks	2.1	2.4	2.6
Frozen Beverages	0.2	0.5	0.9
Hot Beverages	1.4	1.2	1.6
Other Fast Food	0.6	1.2	1.6
Total Non-Gas Merchandise	**100%**	**100%**	**100%**

Fig. 38—Gross Margin Percentage by Product Category — Industry Average

Cooler	
Beer (Hot & Cold)	27%
Soft Drinks (Hot & Cold)	32
Juices	34
Milk & Milk Products	22
Packaged Deli	36
Produce	26
Eggs	23
Frozen	
Frozen Food	37
Ice Cream	39
Ice	53
Room Temp.	
Bread & Cakes	28
Cookies	35
Salty Snacks (Chips, Nuts, etc.)	35
Candy & Gum	41
Groceries	35
Health & Beauty Aids	37
Tobacco	30
Publications	21
Wine/Liquor	30
Automotive/Motor Oil	34
General Merchandise	39
Fast Food	
Sandwiches — Fresh	39
Sandwiches — Frozen	39
Deli Services (excluding sandwiches)	43
Food Cooked On-site	50
Fountain Drinks	58
Frozen Beverages	44
Hot Beverages	61
Other Fast Food	45

Fig. 39—Percentage of Companies Warehousing Specific Product Categories

Dry Grocery	13%
Health and Beauty Aids	6
Dairy	16
Frozen Foods	11
Fast Foods	11
Tobacco	14
Soft Drinks	13

"A" Company Report

The State of the Industry Report specifically focuses on operators of smaller convenience store companies — 1 to 10 stores. This "A" Company Report summarizes the 1985 financial data from 76 operators owning 466 stores. Those surveyed reported key financial and performance indicators pertinent to smaller operations.

We take this opportunity to express our appreciation to everyone who responded to the Association's brief questionnaire. We urge all other operators to participate in future surveys to assure a more complete report for "A" Companies.

Average yearly sales per store, including gas, rose to $1,076,000 from $881,000 in 1984, an increase of 22%. Average non-gas sales per store, however, decreased to $343,000 in 1985 from $357,000 in 1984. The average non-gas gross margin was 29.1% compared to 26.9% in 1984. The average non-gas gross margin for the Group "B", "C", "D", and "E" companies was 32.2% for 1985 and 32.0% in 1984. The "A" stores, therefore, appeared to have closed some of the gap in their gross margin versus that of the larger companies. As also experienced by the larger companies, the "A" stores reported a decrease in average pretax profit, including gas (2.1% in 1985 compared to 2.4% in 1984).

Other income and other expense, as a percent of total sales, approximated 1.7% and 1.4% in 1985 compared to 1.7% and 1.9% in 1984, respectively.

Forty-three percent of the companies responding reported having video games, compared to 66% in 1984. This certainly reflects the fading of the video game craze.

General and administrative expenses were 4.1% of total sales, a decrease from 5.0% in 1984. The reduction in general and administrative expenses paralleled the decrease reported by the larger companies.

"A" Company Gas Operations

Gross margin per gallon of gasoline increased from 6.4 cents in 1984, to 7.6 cents in 1985. As a result, the gross margin percentage rose to 7.6% in 1985. Eighty-eight percent of all "A" stores reporting in 1985 sold gas, up from 84% in 1984.

Shrinkage

Inventory shrinkage directly affects convenience store profitability and continues to be an area of great concern. Our survey indicated that the "A" Companies' inventory shrinkage increased slightly in 1985. Shrinkage as a percentage of non-gas sales was 1.5% in 1981, 1.2% in 1982, 1.0% in 1983, 1.4% in 1984, and increased to 1.5% in 1985.

LIFO

LIFO is an inventory costing technique which charges the most recent cost of goods to cost of sales and thereby reduces the reported profits in an inflationary period. Companies that do not use the LIFO method report illusionary inventory profits, pay taxes on those illusionary profits and consequently reduce their cash flow.

Approximately 57% and 50% of those reporting account for gas and food inventories, respectively, on the LIFO basis.

Fig. 40—"A" Sales and Profitability

	Average Yearly Sales Per Store		Average Non-Gas Gross Margin	Average Pretax Profit Including Gas
	Including Gas	Non-Gas		
1985	$1,076,000	$343,000	29.1%	2.1%
1984	881,000	357,000	26.9	2.4
1983	886,000	326,000	26.9	2.4